

Office of the State Auditor
Division of State Audit

Valley City State University
Valley City, North Dakota

Audit Report for the
Biennium Ended June 30, 2007
Client Code 24200

Robert R. Peterson
State Auditor



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Transmittal Letter

March 6, 2008

The Honorable John Hoeven, Governor
Members of the North Dakota Legislative Assembly
Dr. Ellen Chaffee, President, Valley City State University

We are pleased to submit this audit of Valley City State University for the biennium ended June 30, 2007. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

The in-charge auditor for this audit was Mary Feltman, CPA. John Grettum, CPA was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 239-7289. We wish to express our appreciation to President Chaffee and her staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

Robert R. Peterson
State Auditor

Executive Summary

INTRODUCTION

The historical antecedents of the University were the State Normal School, chartered in the original North Dakota Constitution, the State Teachers College, authorized in 1921 to grant the bachelor's degree, and Valley City State College, so named by the Legislative Assembly in 1963. In 1987 the Legislative Assembly designated the institution as Valley City State University, a regional baccalaureate university of the North Dakota University System. Under the governance of the State Board of Higher Education, the University offers a strong and comprehensive range of academic programs, carefully established within the capabilities and public mission of the institution, which serve the educational needs of a diverse student body, and which are consistent with the standards of academic quality which apply to collegiate education throughout the United States.

An important part of Valley City State University (VCSU) is the availability of technology that has been incorporated into the learning experience. As a "laptop university," full-time VCSU students are issued a laptop computer and have access to a technology environment that includes high-speed wireless network access throughout campus and "smart" classrooms equipped with the latest multimedia technology.

More information may be obtained from Valley City State University's home page at: <http://www.vcsu.edu/>.

RESPONSES TO LAFRC AUDIT QUESTIONS

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies.

1. What type of opinion was issued on the financial statements?

Unqualified.

2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?

Yes.

3. Was internal control adequate and functioning effectively?

Yes.

4. Were there any indications of lack of efficiency in financial operations and management of the agency?

No.

5. *Has action been taken on findings and recommendations included in prior audit reports?*

There were no findings or recommendations in the prior audit report.

6. *Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.*

Yes, a management letter was issued and is included on page 16 of this report, along with management's response.

LAFRC AUDIT COMMUNICATIONS

1. *Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.*

There were no significant changes in accounting policies, contingent liabilities, or significant unusual transactions however; the President of Valley City State University is an ex-officio member of the Board of Directors of the Valley City State University Foundation.

2. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

The most significant accounting estimates used by Valley City State University include: useful lives of capital assets and allowance for uncollectible receivables. Estimated useful lives are used to compute depreciation on capital assets. Management's estimate of the allowance for uncollectible receivables is based on aging categories and past history. We evaluated the key factors and assumptions used to develop the allowances in determining that it is reasonable in relation to the financial statements taken as a whole.

3. *Identify any significant audit adjustments.*

The only significant audit adjustment for our audit period was Posted Audit Adjustment #11 on page 17 of the fiscal year 2006 North Dakota University System audit report.

4. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

5. *Identify any serious difficulties encountered in performing the audit.*

None.

6. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

7. *Identify any management consultations with other accountants about auditing and accounting matters.*

None.

8. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance, Human Resource Management System (HRMS), and Student Administration are high-risk information technology systems critical to Valley City State University.

Background Information

The mission of Valley City State University is to prepare people for life through visionary leadership and exemplary practices in teaching, learning, and service. They do this in an environment that reflects their tradition of personal service, commitment to innovative technology-enriched education, and dynamic learning relationships with community, employers, and society.

Valley City State University's vision is nationally acclaimed for attracting and retaining talented individuals who advance quality learning opportunities and economic growth through technology and innovation.

The purposes of Valley City State University are to:

- Award degrees in education, business, and the liberal arts and sciences;
- Deliver a quality educational experience in an innovative culture and a technologically enhanced environment;
- Serve the best interests of our students, region, and society;
- Lead in effectively applying information media technologies for learning; and
- Promote the appreciation of diversity, a multicultural perspective, and global awareness.

The University regularly reports to the State Board of Higher Education.

More information may be obtained from Valley City State University's home page at: <http://www.vcsu.edu>.

Audit Objectives, Scope, And Methodology

Audit Objectives

The objectives of this audit of Valley City State University for the biennium ended June 30, 2007 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the most important areas of Valley City State University's operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to Valley City State University and are they in compliance with these laws?
3. Are there areas of Valley City State University's operations where we can help to improve efficiency or effectiveness?

Audit Scope

This audit of Valley City State University for the biennium ended June 30, 2007 was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. To meet the objectives outlined above, we:

Audit Methodology

- Prepared condensed financial statements from the data used in the North Dakota University System's financial statement audits and developed a discussion and analysis of the financial statements.
- Tested and analyzed samples of expenses, direct general ledger transactions (ONL's), and receipts.
- Performed detailed analytical procedures related to statement of net asset items, revenue and expenses, and statement of cash flow items.
- Reviewed prior year audit workpapers.
- Interviewed appropriate agency personnel.
- Reviewed Valley City State University written plans and applicable manuals.
- Observed Valley City State University's processes and procedures.
- Reviewed applicable sections in the North Dakota Century Code (NDCC), North Dakota Constitution, and appropriate session laws.
- Reviewed applicable meeting minutes.

Discussion And Analysis

The accompanying financial statements do not have the disclosures required by generally accepted accounting principles (GAAP) and have been prepared in a condensed form to present Valley City State University's financial position and the results of operations in a manner similar to that used for financial reporting in the private sector. Accordingly, the accompanying financial statements are not intended to be presented in accordance with GAAP.

For the biennium ended June 30, 2007, operations of Valley City State University were primarily supported by appropriations from the state's general fund (38%); student tuition and fees (24%); federal grants and contracts (9%); and auxiliary enterprises (14%). This is supplemented by state and local grants and contracts, gifts, and state appropriation for capital assets.

FINANCIAL SUMMARY

Operating revenues consisted primarily of student tuition and fees, as well as federal grants and contracts and auxiliary enterprises. Nonoperating revenues during the audited period included state appropriations, capital grants, and gifts. These revenues remained fairly consistent between fiscal years 2007 and 2006, except state and local grants and contracts decreased \$973,268 and nongovernmental grants and contracts decreased \$373,396. Total revenues were \$14,801,995 for the year ended June 30, 2007 as compared to \$16,400,813 for the year ended June 30, 2006.

The decrease in state and local grants and contracts was primarily due to Valley City State University receiving a \$1 million Center of Excellence grant in fiscal year 2006. The decrease in nongovernmental grants and contracts was primarily because of three grants. \$125K was received in fiscal year 2006 for a Tech Ed City grant; \$141K in Foundation grants was erroneously recorded in fiscal year 2006; and \$50K Bush grant for both fiscal years was received in fiscal year 2006.

Expenses remained fairly constant. Total expenses for Valley City State University were \$15,067,855 for the year ended June 30, 2007 as compared to \$14,884,410 for the prior year.

***ANALYSIS OF SIGNIFICANT VARIANCES BETWEEN FINAL
BUDGETED AND ACTUAL EXPENSES***

Valley City State University had no significant variances for the general fund expenses as reflected on the statement of appropriations.

Financial Statements

STATEMENT OF NET ASSETS

	June 30, 2007	June 30, 2006
ASSETS		
Cash and cash equivalents	\$ 3,852,681	\$ 3,236,056
Investments	1,163,466	989,144
Accounts receivable, net	116,785	112,702
Receivable from component units	33,553	35,283
Due from state general fund	5,031	112,323
Grants and contracts receivables, net	214,648	498,340
Inventories	163,087	183,320
Notes receivable, net	714,282	723,824
Other assets	99,814	93,456
Capital assets, net	7,386,515	7,950,318
Total assets	\$ 13,749,862	\$ 13,934,766
LIABILITIES		
Accounts payable	\$ 493,888	\$ 186,049
Accrued payroll	676,888	589,558
Deferred revenue	62,270	91,450
Deposits	83,299	106,317
Other liabilities	147,026	177,977
Due to others	4,448,805	4,679,869
Total liabilities	\$ 5,912,176	\$ 5,831,220
NET ASSETS		
Invested in capital assets, net of related debt	\$ 3,349,672	\$ 3,523,766
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	459,944	469,872
Expendable:		
Scholarships and fellowships	174,855	152,766
Instructional department uses	850,758	1,146,819
Loans	752,168	743,340
Debt service	500,046	569,786
Unrestricted	1,750,243	1,497,197
Total net assets	\$ 7,837,686	\$ 8,103,546

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	<u>June 30, 2007</u>	<u>June 30, 2006</u>
OPERATING REVENUES		
Student tuition and fees	\$ 3,738,732	\$ 3,716,120
Federal grants and contracts	1,230,899	1,422,613
State and local grants and contracts	185,583	1,158,851
Nongovernmental grants and contracts	44,713	418,109
Sales and services of educational departments	168,571	274,979
Auxiliary enterprises	2,264,778	2,138,690
Other	11,425	10,408
Total operating revenues	<u>\$ 7,644,701</u>	<u>\$ 9,139,770</u>
OPERATING EXPENSES		
Salaries and wages	\$ 8,933,080	\$ 8,731,319
Operating expenses	3,889,967	3,589,959
Data processing	313,245	596,947
Depreciation	798,748	697,685
Scholarships and fellowships	405,321	462,882
Cost of sales and services	514,959	551,023
Total operating expenses	<u>\$ 14,855,320</u>	<u>\$ 14,629,815</u>
Operating loss	<u>\$ (7,210,619)</u>	<u>\$ (5,490,045)</u>
NONOPERATING REVENUES (EXPENSES)		
State appropriations	\$ 5,956,027	\$ 5,883,076
Gifts	720,485	636,244
Investments income	234,309	201,412
Interest on capital asset-related debt	(212,535)	(222,857)
Gain (loss) on capital assets	18,940	(20,655)
Insurance proceeds	112	
Other nonoperating revenues (expenses)	5,596	(11,083)
Net nonoperating revenues	<u>\$ 6,722,934</u>	<u>\$ 6,466,137</u>
(Loss) income before capital grants, gifts, and transfers	<u>\$ (487,685)</u>	<u>\$ 976,092</u>
State appropriations-capital assets	\$ 142,800	\$ 540,311
Capital grants and gifts	79,025	
Total other revenue	<u>\$ 221,825</u>	<u>\$ 540,311</u>
(Decrease) increase in net assets	<u>\$ (265,860)</u>	<u>\$ 1,516,403</u>
NET ASSETS		
Net Assets-beginning of the year	8,103,546	6,587,143
Net Assets-end of the year	<u>\$ 7,837,686</u>	<u>\$ 8,103,546</u>

STATEMENT OF CASH FLOWS

	June 30, 2007	June 30, 2006
CASH FLOWS FROM OPERATING ACTIVITIES		
Student tuition and fees	\$ 3,702,415	\$ 3,676,701
Grants and contracts	1,744,887	2,813,921
Payments to suppliers	(4,353,228)	(4,937,228)
Payments to employees	(8,868,924)	(8,636,687)
Payments for scholarships and fellowships	(405,321)	(462,882)
Loans issued to students	(142,777)	(148,931)
Collection of loans to students	141,187	126,145
Auxiliary enterprise charges	2,266,069	2,144,088
Sales and service of educational departments	178,904	266,085
Cash paid on deposits	(4,372)	(7,454)
Other receipts	2,993	12,462
Net cash used by operating activities	<u>\$ (5,738,167)</u>	<u>\$ (5,153,780)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	\$ 5,956,027	\$ 5,883,076
Grants and gifts received for other than capital purposes	720,485	636,244
Agency fund cash (decrease) increase	(24,591)	16,706
Other nonoperating (expenses) revenue	(25,357)	41,608
Net cash flows provided by noncapital financing activities	<u>\$ 6,626,564</u>	<u>\$ 6,577,634</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital appropriations	\$ 250,092	\$ 481,876
Capital grants and gifts received	25,274	
Purchases of capital assets	(180,587)	(510,358)
Insurance proceeds	112	
Principal paid on capital debt and lease	(209,238)	(250,670)
Interest paid on capital debt and lease	(212,535)	(222,857)
Net cash used by capital and related financing activities	<u>\$ (326,882)</u>	<u>\$ (502,009)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	\$ 573,403	\$ 184,805
Interest on investments	229,432	201,412
Purchase of investments	(747,725)	(149,998)
Net cash provided by investing activities	<u>\$ 55,110</u>	<u>\$ 236,219</u>
Net increase in cash	616,625	1,158,064
CASH - BEGINNING OF YEAR	3,236,056	2,077,992
CASH - END OF YEAR	<u><u>\$ 3,852,681</u></u>	<u><u>\$ 3,236,056</u></u>

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RECONCILIATION OF NET OPERATING REVENUES (EXPENSES) TO

NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES

	June 30, 2007	June 30, 2006
Operating loss	\$ (7,210,619)	\$ (5,490,045)
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities		
Depreciation expense	798,748	697,685
Change in assets and liabilities		
Accounts receivable adjusted for interest receivable	10,092	(23,299)
Grant and contract receivables	283,692	(185,652)
Inventories	20,233	(11,271)
Notes receivable	9,542	30,588
Other assets	(6,358)	4,129
Accounts payable and accrued liabilities adjusted for interest payable	325,899	(236,707)
Accrued payroll	85,981	54,978
Compensated absences	(21,825)	39,654
Deferred revenue	(29,180)	(26,386)
Deposits	(4,372)	(7,454)
Net cash used by operating activities	\$ (5,738,167)	\$ (5,153,780)

SUPPLEMENTAL DISCLOSURE ON NONCASH TRANSACTIONS

Gifts of capital assets	\$ 53,751	
Total non-cash transactions	\$ 53,751	

STATEMENT OF APPROPRIATIONS

For The Biennium Ended June 30, 2007

	Original		Final		Unexpended
Expenses by line item:	Appropriation	Adjustments	Appropriation	Expenses	Appropriation
Operating expenses	\$ 11,806,526	\$ 32,577	\$ 11,839,103	\$ 11,839,103	
Capital assets	508,416		508,416	498,039	\$ 10,377
Capital assets - carryover		83,929	83,929	83,929	
Totals	\$ 12,314,942	\$ 116,506	\$ 12,431,448	\$ 12,421,071	\$ 10,377
Expenses by source:					
General Fund	\$ 12,314,942	\$ 116,506	\$ 12,431,448	\$ 12,421,071	\$ 10,377
Totals	\$ 12,314,942	\$ 116,506	\$ 12,431,448	\$ 12,421,071	\$ 10,377

Appropriation Adjustments:

Operating expenses

The \$32,577 adjustment is a transfer from North Dakota University System contingency fund for disabled student services pursuant to SB 2003 section 8 of the 2005 session laws.

Capital assets - carryover

The \$83,929 adjustment is the prior biennium unspent general fund.

Internal Control

In our audit for the biennium ended June 30, 2007, we identified the following areas of Valley City State University's internal control as being the most important:

Internal Controls Subjected To Testing

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenses.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with laws and legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered significant. We concluded internal control was adequate. Our consideration of internal control would not necessarily disclose all matters that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements that would be material may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control and its operation that we consider to be material weaknesses. However, we noted other matters involving internal control that we have reported to management of Valley City State University in a management letter dated March 6, 2008. See page 16 for management letter.

Compliance With Legislative Intent

In our audit for the biennium ended June 30, 2007, we identified and tested Valley City State University's compliance with legislative intent for the following areas that we determined to be significant and of higher risk of noncompliance:

Legislative Intent Subjected To Testing

- Proper use/approval of clearing account and petty cash/till funds (NDCC 54-06-08.1 and Attorney General's opinion dated September 11, 1987).
- BND used as credit card processing depository (NDCC 54-06-08.2).
- Deposit and expenses of gifts to a state institution (Article IX, Section 1 of the North Dakota Constitution; Attorney General's opinion dated September 13, 1963; NDCC 1-08-02, 1-08-04, 15-10-12, 15-67-01, 15-67-04, 15-67-05, and 15-67-07).
- Fixed asset requirements including record keeping, lease and financing arrangements in budget requests, and lease analysis requirements (NDCC 54-44.1-06, 54-27-21, and 54-27-21.1).
- Inventory records (NDCC 44-04-07).
- Expenses including proper voucher approvals (NDCC 44-08-05.1 and Article X, Section 12, subpart 2 of North Dakota Constitution) and being within budgeted amounts (NDCC 54-44.1-09, Article X, Section 12 of North Dakota Constitution and Attorney General's opinion dated January 6, 1977).
- Travel-related expenses are made in accordance with state statute (NDCC 44-08-04, 44-08-04.1-.5, and 54-06-09 parts 1a, 1b, 3, 4, 5, 6).
- Purchasing including bidding (NDCC 54-44.4-01, 54-44.4-05, 54-44.4-06, 54-44.7-02, 54-44.4-02, 44-08-01, and 48-01.1-03).
- Conflict of Interest (NDCC 12.1-13-03 and 48-02-12).
- Carryover of unexpended appropriations (NDCC 54-44.1-11).
- Adequate blanket bond coverage (NDCC 26.1-21-08).
- Unclaimed property laws (NDCC 47-30.1-02.1, 47-30.1-03.1, 47-30.1-04, and 47-30.1-05).
- Nepotism (NDCC 44-04-09).
- Bond Revenues and Reserves (NDCC 15-55-03 and 15-55-06).
- Misapplication of entrusted property (NDCC 12.1-23-07).

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. Thus, we concluded there was compliance with the legislative intent identified above.

Management Letter (Informal Recommendations)

March 6, 2008

Ms. Trudy Collins
Vice President for Business Affairs
Valley City State University
101 College Street SW
Valley City, ND 58072

Dear Ms. Collins:

We have performed an audit of Valley City State University for the biennium ended June 30, 2007, and have issued a report thereon. As part of our audit, we gained an understanding of Valley City State University's internal control structure to the extent we considered necessary to achieve our audit objectives. We also performed tests of compliance as described in the same report.

Our audit procedures are designed primarily to enable us to report on our objectives including those related to internal control and compliance with laws and regulations and may not bring to light all weaknesses in systems and procedures or noncompliance with laws and regulations which may exist. We aim, however, to use our knowledge of your organization gained during our work to make comments and suggestions which we hope will be useful to you.

In connection with the audit, gaining an understanding of the internal control structure, and tests of compliance with laws and regulations referred to above, we noted certain conditions we did not consider reportable within the context of your audit report. These conditions relate to areas of general business practice or control issues that have no significant bearing on the administration of state, private, or federal funds. We do, however, want to present our recommendations to you for your consideration and whatever follow-up action you consider appropriate. During the next audit we will determine if these recommendations have been implemented, and if not, we will reconsider their status as non-reportable conditions.

The following present our informal recommendations.

TRAVEL

Informal Recommendation 07-1:

VCSU coaches are not required to complete individual travel reimbursement vouchers when traveling with their respective teams. Their expenses are included as part of team travel and charged to account 521105, Travel – Students, rather than being charged as employee expenses. The total expenses charged to account 521105 were over \$118,000 for our two year audit period.

We recommend that VCSU coaches submit a detailed record of travel expenses on a travel reimbursement voucher for all of their travel.

Valley City State University Response:

VCSU agrees with the intent of the recommendation, however, believes the cost of implementation would outweigh the benefit gained by implementation. VCSU will code the coaches' lodging and meals expenses to employee travel codes when those expenses are easily identifiable within team travel invoices.

Auditor's Concluding Comments:

VCSU is responsible for compliance with sound accounting practices and compliance with laws and regulations. They should seek the least costly basis for effective compliance but cost should not prevent the implementation of sound accounting practices and compliance with laws and regulations.

USE, TRANSFER, AND DISPOSAL OF PUBLIC PROPERTY

Informal Recommendation 07-2:

VCSU has adopted SBHE policies and they do not contain a policy prohibiting the disposal, use, or transfer of (any) public property in an unauthorized manner. Although SBHE policy 611.5 is regarding the disposal or transfer of real property and the use of state vehicles, there is no policy that requires written approval and acknowledgement of responsibilities before any equipment can leave the campus.

We recommend that VCSU create and implement policies and procedures regarding the proper disposal, use and transfer of public property, as well as requiring written approval and acknowledgement of responsibilities regarding equipment that leaves the campus.

Valley City State University Response:

VCSU agrees with the recommendation. Currently the VCSU Information Technology Center (ITC) has procedures in place for technology equipment that leaves campus. A computing resources contract is signed by all employees and students before issuance of a laptop computer. The Information Technology Center (ITC) also has a form that is signed by employees and students when checking out equipment from ITC. However a campus wide policy covering the proper disposal, use and transfer of public property is not in place. VCSU will develop and implement policies and procedures regarding the proper disposal, use and transfer of public property.

I encourage you to call me at (701) 239-7289 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,

John Grettum, CPA
Audit Manager